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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FIRST APPELLATE DISTRICT

DIVISION ONE

BANK OF AMERICA, N.A., Plaintiff and Respondent, v. PRITI SHETTY et al., Defendants and Appellants.	A145385 (Napa County Super. Ct. No. 26-44659)

Defendants Priti Shetty and Sandesh Shetty appeal from an amended judgment for amounts due under their guarantees of a loan[1] made to Pooja Oil Company, LLC (Pooja). The amended judgment was entered about five years after the original judgment, which authorized the foreclosure and sale of the property securing the loan and allowed for a postsale deficiency judgment. In 2014, before the bank moved to modify the judgment of foreclosure into a money judgment for the full amount of the outstanding debt, the property securing the loan was sold at a tax sale. The Shettys now argue the bank was estopped from obtaining modification of the judgment. We agree. The bank prejudiced the Shettys by sitting on the judgment for years and declining to move to amend until

[1] Business Loan Center, LLC (BLC) originally made the loan. The loan was later assigned to BLC Funding LLC, and then to LaSalle Bank National Association (LaSalle). Plaintiff Bank of America, N.A. (BofA), became the trustee on the loan after it purchased LaSalle's parent company. BLC remains the beneficiary of record and continues to service the loan on behalf of BofA. For the sake of clarity we refer to these various institutions, collectively, as the bank.

after the security was destroyed. As a result of the bank's actions, the Shettys' subrogation rights were substantially impaired. Accordingly, we reverse.

I. BACKGROUND

In or around November 2005, Pooja borrowed $1.037 million from the bank. The loan was secured by a deed of trust on a gas station and the real property on which it was built. The Shettys guaranteed the loan.

Pooja defaulted on the loan on or around July 2008. The bank subsequently brought a judicial foreclosure action against Pooja, the Shettys, and several other guarantors. The first amended complaint asserted two claims, one for judicial foreclosure against all defendants, and the other for breach of written guarantees. In August 2009, the bank moved for summary judgment on all of its claims. In October 2009, while the motion was pending, the County of Napa issued an abatement order concerning three underground storage tanks on the subject property.

The bank's motion for summary judgment was granted, and the trial court entered a judgment of foreclosure and order of sale on March 12, 2010. The judgment stated Pooja and the Shettys were indebted to the bank for a principal amount of $1,012,103.96, plus accrued interest, accrued late fees, and attorney fees and costs, as well as interest at a rate of 10 percent per annum from the date of the entry of judgment. The judgment also directed the subject property be sold with the proceeds applied to the indebtedness. The court retained jurisdiction to determine the amount of any deficiency after sale and to enter a deficiency judgment.

The bank elected not to sell the property, concluding the estimated costs of further environmental assessments, removal of the underground storage tanks, and environmental fines imposed by Napa County significantly outweighed any return from a foreclosure sale. In May 2014, the property was sold by Napa County at a tax sale due to delinquent real estate taxes in the amount of $101,724.71. The property was sold for $114,300.

In February 2015, almost five years after judgment was entered, the bank moved to amend the judgment to provide for a money judgment against the Shettys in the sum of

$1,839,906.10, plus interest at a rate of 10 percent per annum from April 7, 2015 to the date the amended judgment is entered. In doing so, the bank did not seek a foreclosure deficiency judgment, but instead explicitly sought a judgment against the Shettys to effectuate the trial court's grant of "summary judgment on the second cause of action for breach of written guarantee against the Shettys." The trial court granted the motion on April 23, 2015, and entered the amended judgment on June 16, 2015. The Shettys appealed from both the order granting the motion to amend and the amended judgment.

II. DISCUSSION

The Shettys argue the bank lost the right to have any money judgment other than a deficiency judgment when it elected to proceed by way of judicial foreclosure.[2] The argument has merit. The bank was free to plead inconsistent remedies, including a demand for both a judgment of foreclosure and a money judgment for the full amount of indebtedness. However, once the bank elected a remedy and pursued it to judgment, it could not belatedly request an amendment of the judgment and a change in remedies when such a change would prejudice the Shettys. Principles of estoppel bar such tactics. Accordingly, we must reverse.

As an initial matter, we observe the bank's remedies in this action were limited by the antideficiency statutes. Code of Civil Procedure[3] section 726 provides that "[t]here can be but one form of action for the recovery of any debt or the enforcement of any right secured by mortgage upon real property." (§ 726, subd. (a).) This so-called "one-action rule" generally "compels a secured creditor to exhaust its security in a single judicial action before obtaining a monetary deficiency judgment against the debtor. [Citation.] The purpose of the one action rule is to prevent a secured creditor from enforcing its rights by seeking recourse to more than one remedy, such as by obtaining both a money

[2] The Shettys also argue the trial court lacked jurisdiction to amend the 2010 judgment and any application of the deficiency judgment needed to have been made within three months of the tax sale. The merits of these claims are dubious, but we need not and do not address them.

[3] All statutory references are to the Code of Civil Procedure.

judgment on the mortgage debt and by foreclosing on the mortgage." (*C.J.A. Corp. v. Trans-Action Financial Corp.* (2001) 86 Cal.App.4th 664, 668–669 (*C.J.A.*).)

The one-action rule may be asserted by a debtor as an affirmative defense or it may be raised as a sanction. (*Walker v. Community Bank* (1974) 10 Cal.3d 729, 734.) "If the debtor successfully raises the [one-action rule] as an affirmative defense, the creditor will be forced to exhaust the security before he may obtain a money judgment against the debtor for any deficiency. [Citations.] If the debtor does not raise the [rule] as an affirmative defense, he may still invoke it as a sanction against the creditor on the basis that the latter by not foreclosing on the security in the action brought to enforce the debt, has made an election of remedies and waived the security." (*Ibid.*) The one-action rule does not apply to a creditor's action against a guarantor, and thus a creditor need not exhaust the security before pursuing a guarantor. (*Union Bank v. Gradsky* (1968) 265 Cal.App.2d 40, 43–44, fn. 3 (*Gradsky*).)

Where a secured debt is guaranteed by a third party, the creditor has three options in the event of default. *First*, the creditor may bring an action for judicial foreclosure, joining both the primary obligor on the debt and the guarantor. (*Gradsky, supra*, 265 Cal.App.2d at p. 43.) If the property securing the debt is sold for less than the amount of the outstanding indebtedness, the creditor may seek a deficiency judgment against the debtor and the guarantor. (*Alliance Mortgage Co. v. Rothwell* (1995) 10 Cal.4th 1226, 1236 (*Alliance Mortgage*).) The deficiency judgment is limited to the difference between the amount of the indebtedness and the fair market value of the property as determined by the court, and the debtor has right to redeem the property by paying the foreclosure sale price. (*Ibid.*) *Second*, the creditor may foreclose on the security by way of a nonjudicial foreclosure sale, also known as a trustee's sale. (*Gradsky*, at p. 43.) Unlike judicial foreclosure, a judicial determination of fair value is not required, the debtor does not have a right of redemption, and the creditor may not seek a deficiency judgment against the debtor. (*Alliance Mortgage*, at p. 1236.) *Third*, the creditor may sue the guarantor for the full amount of the unpaid balance of the principal obligation, without first proceeding against either the primary obligor or the

security. (*Gradsky*, at p. 43.) The guarantor then acquires by subrogation all of the creditor's rights against the primary obligor, including the right to pursue judicial or nonjudical foreclosure. (*Id.* at p. 45.)

In a number of cases, courts have considered whether a plaintiff who secured a judgment providing for one of the above remedies could thereafter obtain a modification of the judgment to provide for an alternative remedy. In *Vlahovich v. Cruz* (1989) 213 Cal.App.3d 317 (*Vlahovich*), the creditor obtained a judgment of foreclosure and, about three years later, moved to amend the judgment to allow for a private trustee's sale to recover the balance due. (*Id.* at p. 320.) The order granting the motion was reversed on appeal. (*Id.* at p. 323.) The court held: "A litigant will be held to his choice of remedies if 'having full knowledge of all of the facts has elected one of two inconsistent remedies and *pursues it to judgment*.' " (*Ibid.*) The creditor presumably pursued judicial foreclosure because he expected it would be necessary to obtain a deficiency judgment, and later determined nonjudicial foreclosure was more advantageous because the security had appreciated in value. (*Ibid.*) The court explained: "[I]t would be extremely unfair to permit [the creditor] to proceed to judgment in a judicial foreclosure action—thereby preserving his right to a deficiency judgment—and then, three years later, change his course of action to gain the benefit of the inflated value of San Francisco real estate and at the same time obliterate [the debtor]'s extant right of redemption." (*Ibid.*, fn. omitted.)

A similar conclusion was reached in *C.J.A.*, *supra*, 86 Cal.App.4th 664. There the trial court entered a judgment of foreclosure in favor of the plaintiff and retained jurisdiction to enter a deficiency judgment. (*Id.* at pp. 666–667.) Over a year later, after a senior lienholder foreclosed on the subject property, the plaintiff moved to convert the judgment into a money judgment for the full amount of the debt. (*Id.* at p. 667.) Examining *Vlahovich*, the court found a central issue was "the prejudice to the debtor caused by the creditor's belated change of remedy. '[T]he modern tendency is to explain election in terms of estoppel, i.e., to take into consideration not merely the plaintiff's manifestation of choice but also its effect on the defendant. Hence, despite a clear manifested intention to pursue one of two inconsistent remedies, the plaintiff may

thereafter seek the other remedy if the change will not work a substantial injury to the adverse party. [Citation.] But if the change will for some reason operate to the prejudice of the defendant, the plaintiff's new remedy is barred, because his 'election' has continued to the point where he is estopped to change his remedy.' " (*C.J.A.*, at p. 670.)

Applying these principles to the facts of the case, the court found the plaintiff was estopped because a belated change of remedy was unfair to the defendants. (*C.J.A.*, *supra*, 86 Cal.App.4th at pp. 670–671.) "Most fundamentally," changing the judgment of foreclosure to a money judgment summarily eliminated the debtor's rights under section 726, specifically its right to a fair value hearing and its right to redeem the property. (*C.J.A.*, at p. 671.) Further, the defendants were prejudiced by the modification of the judgment to the extent they had expended attorney fees and costs in defending an action for judicial foreclosure, not to a claim for a money judgment. (*Ibid.*) Finally, allowing the plaintiff to modify the final judgment to obtain a completely different remedy did an injustice to the strong policy favoring finality of actions. (*Ibid.*)

The Second Appellate District also invoked the principles of estoppel in *Gradsky*, *supra*, 265 Cal.App.2d 40. In that case, the debtor defaulted on a building loan agreement and the creditor bank commenced nonjudicial foreclosure and caused the security to be sold at a trustee's sale. (*Id.* at pp. 41–42.) The creditor then sued the guarantor on the note to recover the deficiency. (*Id.* at p. 42.) The order sustaining the guarantor's demurrer to the creditor's complaint was affirmed on appeal. (*Id.* at p. 41.) The court noted (1) a guarantor may pay the primary obligor's debt and, by way of subrogation, obtain the creditor's rights against the debtor, including the right to foreclose on the security; and (2) a creditor, as well as a guarantor standing in the creditor's shoes, cannot obtain a deficiency judgment against a debtor if the creditor elects to pursue nonjudicial foreclosure. (*Id.* at pp. 44–46.) Thus, where a lender pursues nonjudicial foreclosure, it effectively destroys the guarantor's subrogation rights against the debtor. (*Id.* at pp. 46–47.) The court concluded that because only the creditor can preserve the guarantor's subrogation rights, the creditor is estopped from pursuing the guarantor if it

elects a remedy, such as nonjudicial foreclosure, which destroys those rights.[4] (*Gradsky*, at pp. 46–47.)

We conclude estoppel also applies in the instant action. Modifying a five-year-old judgment of foreclosure to a money judgment substantially impaired the Shettys' subrogation rights. Had the bank obtained a money judgment against the Shettys in the first instance, the Shettys would have stepped into the shoes of the bank, and they could have pursued a judicial foreclosure action against Pooja. Alternatively, the Shettys could have commenced nonjudicial foreclosure proceedings. Either way, the Shettys would have had the opportunity to foreclose on the security and use the proceeds to offset the bank's money judgment. But the bank's actions effectively precluded the Shettys from taking advantage of the security. The bank initially secured a judgment of foreclosure, meaning the Shettys had no subrogation rights. Instead of proceeding with a foreclosure and seeking a deficiency judgment,[5] the bank sat on its rights for five years. Meanwhile, the subject property was sold by the county at a tax sale. After the security was destroyed, the bank moved to amend the judgment to award against the Shettys the full amount of the outstanding indebtedness based on the bank's contract cause of action. The bank had a duty to the Shettys not to impair their remedies against Pooja. (*Gradsky*, *supra*, 265 Cal.App.2d at p. 46.) The bank breached that duty by obtaining a foreclosure

[4] The court also found the guarantor had not waived an estoppel defense. (*Gradsky*, *supra*, 265 Cal.App.2d. at p. 48.) The language of the guarantee agreement did not specifically waive a defense based upon an election of remedies, and the court would "not strain the instrument to find that waiver by implication." (*Ibid.*) It has since been held the protection afforded to guarantors by *Gradsky* may be waived by contract. (*Mariners Sav. & Loan Assn. v. Neil* (1971) 22 Cal.App.3d 232, 235–236.) As set forth below, we find no waiver here.

[5] We need not and do not decide whether the bank could have successfully obtained a deficiency judgment.

judgment, sitting on its rights for five years, and then seeking a different remedy, a money judgment based on the contract claim, after the security was destroyed.[6]

The bank's arguments on appeal are unavailing. As an initial matter, the bank attempts to distinguish the instant action from *C.J.A.*, *supra*, 86 Cal.App.4th 664. The bank argues that, unlike the creditor in *C.J.A*, it did not pursue inconsistent remedies or pursue one to the exclusion of the other. It is true the bank asserted claims for both judicial foreclosure and breach of written guaranties from the outset of the litigation. But contrary to the bank's contentions, judicial foreclosure and a money judgment for the full amount of the outstanding debt are not consistent remedies, as awarding both would amount to double recovery. And the bank elected one over the other when it pursued its claim for judicial foreclosure to judgment and then sat on that judgment for five years. The bank has cited no authority, nor are we aware of any, that holds a plaintiff only elects a remedy when it executes a judgment.

The bank further argues the equitable considerations that influenced the *C.J.A.* court are not present here because the Shettys are guarantors, not primary obligors. First, the bank contends that, unlike the debtors in *C.J.A.*, the Shettys did not have a right to a fair value hearing under section 726. Second, the bank asserts the one-action rule does not apply to guarantors, so it was free to pursue the Shettys without first exhausting the security. However, even if the Shettys did not have a right to a fair value hearing, the bank substantially prejudiced the Shettys by waiting five years to amend the judgment and allowing the security to be sold at a tax sale in the interim. As to the second point, we agree the Shettys could not invoke the one-action rule as a defense. But our decision is based not on the provisions of the antideficiency statutes but on principles of estoppel. We also observe there is a significant difference between suing a guarantor without first exhausting the security and pursuing a guarantor after allowing the security to be destroyed.

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[6] The value of the security may have been significantly impaired by environmental contamination. But as evidenced by the fact the property was sold for $114,300 at a tax sale, that security was still worth something.

We next reject the bank's contention the Shettys irrevocably waived any guarantor defenses by failing to assert them in their answer or opposition to the bank's 2009 motion for summary judgment. The dispute here turns on whether it was appropriate to amend the judgment of judicial foreclosure to provide for a money judgment against the Shettys. The Shettys could not have predicted the bank would move to amend the judgment when they filed their answer and responded to the motion for summary judgment. Nor could they have predicted the bank would sit on its judgment for five years while the underlying security was sold at a tax sale. The bank is essentially arguing the Shettys forever waived their arguments concerning election of remedies by failing to object to something that had not yet occurred. The contention is disingenuous at best. "Waiver is the intentional relinquishment of a *known* right." (*Cathay Bank v. Lee* (1993) 14 Cal.App.4th 1533, 1539.) Absent a crystal ball, the Shettys could not have known the bank would attempt to change their election of remedies after obtaining a judgment.

The bank asserts the Shettys had reason to challenge its conduct earlier because the bank asserted a separate and independent claim for breach of written guarantee and moved for summary adjudication of that claim. But there does not appear to be any dispute that a judgment on the breach of written guarantee claim would have been appropriate in the first instance. If such a judgment had been entered, the Shettys could have foreclosed on the collateral and used the proceeds to offset the bank's judgment. The issue is that the bank elected a judgment of judicial foreclosure and then later moved to convert it into a money judgment after the collateral was sold at a tax sale. Once again, the bank is essentially arguing we should find a waiver because the Shettys failed to predict the bank would later attempt to elect two inconsistent remedies. We decline to do so.

At oral argument, the bank asserted the Shettys waived various surety defenses when they executed the unconditional guarantee. The bank forfeited this argument by

failing to raise it with the trial court or in its appellate briefing.[7] In any event, we are not persuaded. As discussed above, waiver is the knowing and intentional forfeiture of a right. (*Cathay Bank v. Lee*, *supra*, 14 Cal.App.4th at p. 1539.) " 'The burden is on the party claiming the waiver to prove it by clear and convincing evidence that " 'does not leave the matter doubtful or uncertain . . . .' " ' [Citation.] Waiver requires ' "sufficient awareness of the relevant circumstances and likely consequences." ' [Citation.] [¶] These principles emphasize actual knowledge and awareness of what is being waived, and require resolution of doubts against waiver." (*Ibid*.) Courts will not find a waiver by implication. For example, in *Gradsky*, the court declined to infer a waiver where the guarantee agreement did not specifically discuss "the guarantor's defense based upon an election of remedies which destroys both the guarantor's subrogation rights and his right to proceed against the principal obligor for reimbursement." (*Gradsky*, *supra*, 265 Cal.App.2d 40, 48.)

Likewise, we decline to find a waiver by implication here. The guarantee agreement states the Shettys waive all rights to require "presentment, protest, or demand upon [Pooja]," to "[r]edeem any [c]ollateral before or after Lender disposes of it," and to require a valuation of the collateral. The Shettys also waived defenses based on claims that the bank impaired the collateral, did not dispose of any of the collateral, did not conduct a commercially reasonable sale, did not obtain the fair market value of the collateral, and impaired the Shettys' suretyship rights, among other things. However, the Shettys did not expressly waive any defenses based on estoppel, election of remedies, or the impairment of their subrogation rights. Absent such an express waiver, we decline to infer one.

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[7] In a footnote in its respondent's brief, the bank asserts it *would have* raised the issue of the Shettys' contractual waiver had they raised various defenses earlier. As discussed above, the Shettys had no reason to assert an election of remedies defense earlier as they could not have predicted the bank would elect one remedy and then later change course and elect another. And nothing precluded the bank from asserting this argument in their briefing on the motion to amend the judgment or their appellate briefing.

In sum, we conclude the bank was estopped from obtaining an amendment of the judgment. By waiting five years to seek such an amendment, as well as waiting until after the underlying security was destroyed, the bank significantly impaired the Shettys' subrogation rights.

III. DISPOSITION

We reverse and remand to the trial court with directions that it vacate its order modifying the judgment and reinstate the prior judgment of judicial foreclosure. The Shettys shall recover their costs on appeal.

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Margulies, J.

We concur:

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Humes, P.J.

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Banke, J.

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